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DEFENSE HEALTH PROGRAM FUNDS ADMINISTERED AS
PART OF THE TRICARE PROGRAM

Report No. D-2001-110

April 30, 2001

Office of the Inspector General
Department of Defense

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Acronyms

CHAMPUS	Civilian Health and Medical Program of the Uniformed Services
CPIRI	CHAMPUS Price Inflation Reimbursement Index
DHP	Defense Health Program
MCS	Managed Care Support
PBD	Program Budget Decision
TMA	TRICARE Management Activity



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
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April 30, 2001

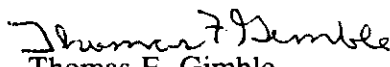
MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)
ASSISTANT SECRETARY OF DEFENSE (HEALTH
AFFAIRS)

SUBJECT: Audit Report on the Defense Health Program Funds Administered as Part
of the TRICARE Program (Report No. D-2001-110)

We are providing this audit report for information and use. We performed the audit in response to a congressional request. We considered management comments on a draft of this report in preparing the final report.

Comments on the draft report conformed to the requirements of DoD Directive 7650.3 and left no unresolved issues. Therefore, no additional comments are required.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. Brian M. Flynn at (703) 604-9489 (DSN 664-9489) (bflynn@dodig.osd.mil) or Mr. Byron B. Harbert at (303) 676-7405 (DSN 926-7405) (bharbert@dodig.osd.mil). See Appendix B for the report distribution. The audit team members are listed inside the back cover.


Thomas F. Gimble
Acting
Deputy Assistant Inspector General
for Auditing

Office of the Inspector General, DoD

Report No. D-2001-110

(Project No. D2000FD-0256)

April 30, 2001

Defense Health Program Funds Administered as Part of the TRICARE Program

Executive Summary

Introduction. In the DoD Appropriations Act for FY 2000, Congress appropriated \$11.15 billion for the Defense Health Program. On July 13, 2000, Congress enacted Public Law No. 106-246, "Making Appropriations for Military Construction, Family Housing, and Base Realignment and Closure for the Department of Defense for Fiscal Year Ending September 30, 2001, and for Other Purposes." Public Law No. 106-246 appropriated an additional \$1.3 billion to cover critical shortfalls in funding managed care support contracts. In House Conference Report No. 106-710, which accompanied Public Law No. 106-246, conferees directed the Inspector General, DoD, in coordination with the General Accounting Office, to examine the fund control practices of the TRICARE (the military health care system) program. In addition, DoD was directed to report to the congressional Defense committees within 60 days after enactment on whether DoD violated fiscal law or departmental regulations related to the shortfalls. Public Law No. 106-246, section 105, specifically appropriated \$615.6 million of the \$1.3 billion for the Defense Health Program with the following stipulations specified in section 106.

- In section 106(a)(1), Congress earmarked \$90.3 million to fund the unanticipated increases in TRICARE contract costs that were properly chargeable to FYs 1998 and 1999.
- In section 106(a)(2), Congress earmarked \$525.3 million to fund the unanticipated increases in TRICARE contract costs that were properly chargeable to FYs 2000 and 2001.
- In section 106(b), DoD was to notify the congressional Defense committees before charging an obligation or making an adjustment.
- In section 106(c), DoD was to submit a report to the congressional Defense committees on the obligations made no later than 30 days after the end of FY 2000.

Objective. Our objective was to evaluate the fund control practices of the TRICARE program related to the unanticipated increases covered by Public Law No. 106-246, sections 105 and 106.

Results. We could not fully evaluate the fund control practices of the TRICARE program related to the unanticipated increases covered by Public Law No. 106-246, sections 105 and 106. TRICARE had obligated \$569.7 million of the \$615.6 million appropriated by Congress to settle numerous claims as of January 31, 2001. Many claims were settled under a global settlement; therefore, a clear audit trail was not available to determine whether TRICARE maintained effective fund controls and accountability over the obligations related to the unfunded requirements. The following is a list of the \$480.2 million of obligations that we could identify by specific purpose, amount, and line(s) of accounting made against sections 105 and 106.

- About \$4.6 million of the \$20.8 million obligated against the \$90.3 million authorized in section 106(a)(1) could be traced to specific purposes (a bid price adjustment) as of January 31, 2001.
- About \$475.6 million of the \$525.3 million authorized in section 106(a)(2) could be traced to specific purposes as of January 31, 2001. Even then, those purposes were not as originally identified for funding and were not, in some cases, unanticipated.

Regarding section 106(b), we determined that DoD notified the congressional Defense committees by October 30, 2000, of its intent to obligate \$540 million to cover managed care support contract costs. However, as of April 5, 2001, DoD had not submitted its report on the amounts obligated, as required by section 106(c). In addition, as of April 5, 2001, DoD had not provided its report to Congress on whether TRICARE had violated fiscal law or departmental regulations related to the critical shortfalls in funding. The absence of those two DoD reports affected our ability to determine what DoD had established as its baseline for evaluating any potential violations of fiscal law and departmental regulations. See the Finding section for details on the audit results.

Management Comments. Although no comments were required, the Acting Assistant Secretary of Defense (Health Affairs) responded to a draft of this report and stated that he concurred overall with the finding and conclusions in the draft report. He also stated that the draft report accurately represented the identification, validation, and use of the \$615.6 million portion of the FY 2000 Defense Health Program Emergency Supplemental funding. See the Management Comments section for the complete text of the comments.

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Background

In the DoD Appropriations Act for FY 2000, Congress appropriated \$11.15 billion for the Defense Health Program (DHP). On July 13, 2000, Congress enacted Public Law No. 106-246, "Making Appropriations for Military Construction, Family Housing, and Base Realignment and Closure for the Department of Defense for Fiscal Year Ending September 30, 2001, and for Other Purposes" (the Act). The Act appropriated an additional \$1.3 billion to cover critical shortfalls in managed care support (MCS) contracts. In House Conference Report No. 106-710, which accompanied the Act, conferees directed the Inspector General, DoD, in coordination with the General Accounting Office, to examine the fund control practices of the TRICARE (the military health care system) program. In addition, DoD was directed to report to the congressional Defense committees within 60 days after enactment on whether DoD violated fiscal law or departmental regulations related to the shortfalls. The Act, section 105, specifically appropriated \$615.6 million of the \$1.3 billion for the DHP with the following stipulations specified in section 106.

- In section 106(a)(1), Congress earmarked \$90.3 million to fund the unanticipated increases in TRICARE contract costs that were properly chargeable to FYs 1998 and 1999.
- In section 106(a)(2), Congress earmarked \$525.3 million to fund the unanticipated increases in TRICARE contract costs that were properly chargeable to FYs 2000 and 2001.
- In section 106(b), DoD was to notify the congressional Defense committees before charging an obligation or making an adjustment.
- In section 106(c), DoD was to submit a report to the congressional Defense committees on the obligations made no later than 30 days after the end of FY 2000.

Origin of the Act. DoD did not formally request the appropriation made in the Act. Rather, Congress made the appropriation after hearing testimony from DoD officials. In February and March 2000, the Secretary of Defense, Deputy Secretary of Defense, Under Secretary of Defense (Comptroller), and Assistant Secretary of Defense (Health Affairs) testified before various Senate and House of Representatives committees and subcommittees that DoD needed to amend the FY 2001 budget. DoD officials particularly sought a reprogramming of \$228.2 million from the Services and identified an additional \$626.5 million necessary to pay MCS contract claims that were not included in the FY 2001 President's Budget. According to the testimony, approximately \$626.0 million was needed to fund the pharmacy bid price adjustment that Congress directed in the FY 2000 Defense Authorization Act, Public Law No. 106-65, section 701, October 5, 1999, and to settle additional claims covering MCS contract costs from FYs 1998 through 2001.

Background on the Testimony. The DoD testimony and funding requirements that were presented to Congress related to Program Budget Decision (PBD) 041, which sought to amend the FY 2001 President's Budget. The Deputy Secretary of Defense approved PBD 041 on December 20, 1999. PBD 041 included a reprogramming of \$228.2 million from the Services to cover shortfalls in funding military treatment facility pharmacy costs and deferred a decision on providing additional funds to pay for what were termed as "uncertain" liabilities related to MCS contracts. DoD deferred the decision on requesting additional funds to cover MCS contract shortfalls until the Government liability had been firmly determined. DoD did not submit the reprogramming to Congress. Instead, Congress appropriated \$615.6 million to cover the reported MCS contract shortfalls for FYs 1998 through 2001, totaling \$387.6 million, and the \$228 million that would have been reprogrammed from the Services.

MCS Contract Shortfalls. TRICARE first recognized a \$626.5 million budget shortfall for covering FY 1998 through FY 2001 MCS contract costs in late calendar year 1999 or early 2000. In October 1999, TRICARE personnel requested MCS contractors to provide information on potential claims and requests for equitable adjustments during a TRICARE Access Summit in Denver, Colorado. We believe those claims constituted the "uncertain" requirements mentioned in PBD 041. Table 1 lists the original contract issues that were raised as a result of the TRICARE Access Summit. The amounts shown are the Government's estimates.

Table 1. Initial Undated Requirements

(in millions)

Bid Price Adjustment and Request for Equitable Adjustment Issues

<u>Funding Issue</u>	<u>Total FYs 1998-2001</u>
CHAMPUS ¹ Price Inflation Reimbursement Index (CPIRI)	\$ 69.0
Resource sharing	68.5
Telephone consultations ²	110.0
Meridian audit ³	85.8
Pharmacy	228.2
Contract extensions	65.0
Total initial requirement	\$ 626.5

¹ Civilian Health and Medical Program of the Uniformed Services.

² Contractors claimed that they should have been compensated for telephone consultations provided to health care beneficiaries.

³ The TRICARE Management Activity contracted with Meridian to perform audits of health care claims processed by the MCS contractors. In certain instances, the audits disclosed that providers under contract had been underpaid and the contractors were entitled to additional payment.

As of July 13, 2000, however, the issues to be resolved changed significantly, although the total amount decreased by \$0.9 million (Table 2). For example, the CPIRI issue was no longer listed as part of the \$625.6 million shortfall, while the bid price adjustment in regions 3 and 4 emerged.

Table 2. July 13, 2000 Requirements (in millions)	
Bid Price Adjustment and Request for Equitable Adjustment Issues	
<u>Funding Issue</u>	<u>Total FYs 1998-2001</u>
Bid Price Adjustment #3, Regions 3,4	\$ 67.2
Resource sharing	22.5
Telephone consultations	119.5
Meridian audit	46.8
Pharmacy	281.8
Contract extensions	87.8
Total requirement	\$ 625.6

And as of September 13, 2000 (Table 3), while the issues marginally changed, the total amount increased by \$94.0 million and the CPIRI issue reemerged.

Table 3. September 13, 2000 Requirements (in millions)	
Bid Price Adjustment and Request for Equitable Adjustment Issues	
<u>Funding Issue</u>	<u>Total FYs 1998-2001</u>
CHAMPUS Price Inflation Reimbursement Index (CPIRI)	\$120.3
Bid Price Adjustment #3, Regions 3,4	67.2
Resource sharing	22.5
Telephone consultations	105.5
Meridian audit	46.2
Pharmacy	270.1
Contract extensions	87.8
Total requirement	\$719.6

Tables 1–3 reflect the changes in the funding issues and amounts that affected the TRICARE MCS contract program from late 1999 to September 13, 2000. According to a TRICARE Management Activity (TMA) representative, those changes were the result of ongoing negotiations with MCS contractors.

Objective

Our objective was to evaluate the fund control practices of the TRICARE program related to the unanticipated increases that were covered by sections 105 and 106 of the Act. See Appendix A for a discussion of the audit scope and methodology and for prior coverage.

TRICARE Fund Control Practices

We could not fully evaluate the TRICARE fund control practices related to the unanticipated increases that were covered by sections 105 and 106 of the Act. TRICARE had obligated \$569.7 million of \$615.6 million appropriated by Congress to settle numerous MCS contract claims as of January 31, 2001. However, TRICARE did not use all of the funds for the purposes originally identified. In addition, many claims were settled under a global settlement; therefore, a clear audit trail was not available to determine whether TRICARE maintained effective fund controls and accountability over the obligations related to the unfunded requirements. Moreover, DoD had not complied with the legislation by providing its report on the amount of obligations incurred as of October 30, 2000, as required by section 106(c), and its report on whether TRICARE violated fiscal laws or departmental regulations by September 13, 2000, as required in the Conference Report. As of April 5, 2001, according to a TMA representative, the two reports were awaiting final decisions on how to best apply the additional resources, the outcome of the global settlement, and DoD approval of the recommended use of the funds.

TRICARE did not use all of the funds for the purposes originally identified because the requirements changed during ongoing negotiations with the contractors and because many of the issues originally identified by the contractors were folded into the global settlement. TRICARE personnel attempted to negotiate and settle claims as the contractors presented the issues, which resulted in the shift in requirements. A clear audit trail was not available because TRICARE used a global settlement to negotiate a number of contract change orders, requests for equitable adjustment, and other claims. The global settlement did not separately identify the specific issues, amounts paid, and applicable line(s) of accounting.

As a result, we were unable to fully examine the fund control practices related to the unanticipated increases in the MCS contract requirements that generated the funding in sections 105 and 106 of the Act. The absence of the two DoD reports to Congress further impeded our ability to determine what DoD and TRICARE established as a baseline for evaluating any potential violations of fiscal law and departmental regulations.

Obligations Traceable to the Appropriation

As of January 31, 2001, TRICARE had obligated \$569.7 million of \$615.6 million to settle numerous MCS contract claims. However, we were able to match only \$480.2 million of the \$569.7 million in obligations to the specific issues that TRICARE had identified as unfunded requirements. The \$480.2 million included \$4.6 million in obligations made under section 106(a)(1) of the Act, while the balance, \$475.6 million, was obligated

under section 106(a)(2). The remaining \$89.5 million was used to pay agreements reached in the global settlement, where the specific purposes, amounts, and line(s) of accounting were not separately identifiable. Specifically, the \$480.2 million was matched as follows.

- About \$4.6 million of the \$20.8 million obligated against the \$90.3 million authorized in section 106(a)(1) could be traced to specific purposes (a bid price adjustment) as of January 31, 2001.
- About \$475.6 million of the \$525.3 million authorized in section 106(a)(2) could be traced to specific purposes as of January 31, 2001. Even then, those purposes were not as originally identified for funding and were not, in some cases, unanticipated. Those purposes included the settlement of:
 - pharmacy bid price adjustments, \$135.5 million;
 - regular bid price adjustments, \$125.0 million;
 - resource sharing, \$8.8 million;
 - mental health claims, \$5.1 million;
 - other (excess claims volume), \$1.2 million; and
 - the exercise of contract options, \$200.0 million.

Of those obligations listed, two of the six purposes (regular bid price adjustments and contract options) totaling \$325.0 million should have been anticipated and requested in the President's Budget. According to a TMA representative, those purposes were anticipated; however, the funds that were reserved for those purposes were used to fund the military treatment facility requirements and the bid price adjustments were higher than anticipated in the President's Budget. The representative stated that she believed the Conference Report authorized the use of section 106(a)(2) funds for the contract options and regular bid price adjustments. In our opinion, the Conference Report and the legislation do not appear to be fully compatible. The representative also stated that the \$135.5 million in pharmacy bid price adjustments was an unanticipated increase created by the additional pharmacy benefit enacted in the FY 2000 Defense Authorization Act. The remaining \$15.1 million related to unanticipated increases in MCS contract costs that were individually settled requests for equitable adjustments.

Effect of the Global Settlement

Approximately \$89.5 million of the \$569.7 million was paid to liquidate numerous change orders, requests for equitable adjustments, and other claims. Those agreements included settlement of the telephone consultation and Meridian audit issues. However, the global settlement did not provide a clear delineation of the specific purpose, amount, and line(s) of accounting that applied to sections 105 and 106 of the Act. In addition, TRICARE personnel stated that during the negotiation of the global settlement both parties might have

agreed to drop or modify some issues while settling others. A global settlement is an acquisition practice that brings many different issues to resolution. However, the method limits the management visibility and accountability for the individual issues covered in the settlement by specific amount and line(s) of accounting. For example, a global settlement might include different change orders, requests for equitable adjustment, and other claims that cut across different fiscal year appropriations. Unless the global settlement clearly delineates each agreement by amount and fiscal year line(s) of accounting, normal fund control visibility is not maintained.

Summary

Because of the changing MCS contract requirements, we could not fully evaluate the TRICARE fund control practices related to the use of funds made available under sections 105 and 106 of the Act. However, we can generally conclude that TRICARE used the funds to pay for MCS contract services. A number of the requirements were not foreseeable, and even though TRICARE personnel knew of potential liabilities, the MCS contractors controlled when the claims were submitted for negotiation and settlement. Regarding the use of global settlements, unless the contract documents (such as negotiation memorandums) clearly detail the issues, amounts, and line(s) of accounting related to each item, normal fund control visibility is not maintained.

Management Comments

Although no comments were required, the Acting Assistant Secretary of Defense (Health Affairs) responded to a draft of this report and stated that he concurred overall with the finding and conclusions in the draft report. He also stated that the draft report accurately represented the identification, validation, and use of the \$615.6 million portion of the FY 2000 Defense Health Program Emergency Supplemental funding. For the full text of the comments, see the Management Comments section of the report.

Appendix A. Audit Process

Scope and Methodology

Work Performed. We reviewed the TRICARE Directorate of Resource Management initial budget estimate that supported the testimony presented to various Senate and House of Representatives committees and subcommittees that led to the eventual enactment of Public Law No. 106-246. Using the revised estimate, dated July 13, 2000, that TRICARE provided as support for the final issues that would be covered by the emergency appropriation, we attempted to obtain copies of the contract files related to the negotiation and settlement of those contracting issues. We subsequently determined that the documentation received did not completely support budget shortfalls reported by DoD to Congress and the intended uses of the emergency appropriation. Consequently, we requested additional documents and met with personnel from the Office of the Under Secretary of Defense (Comptroller), Office of the Assistant Secretary of Defense (Health Affairs), and TMA to discuss more fully the circumstances surrounding the enactment of the legislation and its terms and conditions. Based on those discussions and our review of the additional documents provided to us, we reduced the scope of our audit to examine the end uses of the appropriation. We also did not review the management control program.

Use of Computer-Processed Data. Computer-processed data were not used in this audit.

Audit Type, Dates, and Standards. We performed this financial-related audit from August 2000 through March 2001 in accordance with audit standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD.

Contacts During the Audit. We visited or contacted individuals and organizations within the DoD. Further details are available on request.

Prior Coverage

The General Accounting Office and the Inspector General, DoD, have conducted prior audits of TRICARE and the Defense Health Program. General Accounting Office reports can be accessed on the Internet at <http://www.gao.gov>. Inspector General, DoD, reports can be accessed on the Internet at <http://www.dodig.osd.mil/audit/reports>.

Appendix B. Report Distribution

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Acting Assistant Secretary of Defense (Health Affairs) Comments



HEALTH AFFAIRS

THE ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, D. C. 20301-1200

APR 23 2001

MEMORANDUM FOR DEPARTMENT OF DEFENSE INSPECTOR GENERAL
ASSISTANT INSPECTOR GENERAL FOR AUDITING
DIRECTOR, FINANCE AND ACCOUNTING DIRECTORATE

SUBJECT: Draft Report on Audit of Defense Health Program Funds Administered as Part of the
TRICARE Program (Report No. D2000FD-0256)

Thank you for the opportunity to review and provide comments on the draft report, "Defense Health Program Funds Administered as Part of the TRICARE Program." The following are my comments on the draft report.

Overall, we concur with the findings and conclusions detailed in the draft report. Recommended technical corrections and comments on the draft report are provided (attached) for consideration in adding to the Final Report.

The Department believes the draft report accurately represents TMA's identification, validation and use of the \$615.6 million portion of the FY00 DHP Emergency Supplemental funding. Within the capability of the existing accounting system the Department utilizes, full access to accounting records and contracting documentation was provided to allow the review and validation of obligations of the emergency supplemental funding.

My points of contact are COL David Daigh at (703) 681-7894, ext. 1219 and Mr. Gunther J. Zimmerman (GAO/IG Liaison) at (703) 681-7889, ext. 1229.

A handwritten signature in cursive script, appearing to read "J. Jarrett Clinton".

J. Jarrett Clinton, MD, MPH
Acting Assistant Secretary

Attachment:
As stated

**DoD IG DRAFT REPORT – DATED APRIL 6, 2001
(D2000FD-0256)
Agency Comments on Draft Audit Report, “Audit of Defense Health Program Funds
Administered as Part of the TRICARE Program”**

DEPARTMENT OF DEFENSE COMMENTS

TECHNICAL CHANGES:

- Page i. First paragraph (Introduction), third sentence. “Public Law No. 106-246 appropriated an additional \$1.3 billion to cover critical shortfalls in funding managed care support contracts.” Comment. In addition to directing the funding for MCS requirements the report language of the FY2001 MILCON Appropriation Act also directed that the funding could be used for other MHS requirements. **Recommend** the sentence be modified to read “Public Law No. 106-246 appropriated an additional \$1.3 billion to cover critical shortfalls in funding managed care support contracts and other DHP funding requirements.”
- Page 2. Second paragraph, second sentence. “In October 1999, TRICARE personnel requested MCS contractors to provide information on potential claims and request for equitable adjustments during a TRICARE Access Summit in Denver, CO.” Comment. In October 1999, TRICARE personnel requested the MCS contractors identify their potential claims and REAs on behalf of the Assistant Secretary of Defense (Health Affairs). **Recommend** the sentence be modified to read “In October 1999, TRICARE personnel and the Assistant Secretary of Defense (Health Affairs) requested MCS contractors to provide information on potential claims and requests for equitable adjustments during a TRICARE Access Summit in Denver, CO.”
- Page 4. First paragraph, first sentence. “We could not fully evaluate the TRICARE fund control practices related to the unanticipated increases that were covered by sections 105 and 106 of the Act.” Comment. Sentence should indicate that the analysis could not be accomplished for the “specific” increases related to the funds provided by emergency supplemental. **Recommend** the sentence be modified to read “We could not fully evaluate the TRICARE fund control practices related to the specific unanticipated increases that were covered by sections 105 and 106 of the Act.”
- Page 6. Second paragraph, first sentence. “TRICARE fund control practice could not be fully examined related to the use of funds made available under sections 105 and 106 of the Act because of the changing MCS contract requirements.” Comment. The sentence does not identify the important reason why the MCS contract requirements changed. **Recommend** the sentence be modified to read “TRICARE fund control practice could not be fully examined related to the use of funds made available under sections 105 and 106 of the Act because of the changing MCS contractor requirements from initial estimates to negotiated settlements six months later.”

COMMENTS ON SUMMARY

In the Summary of the Draft Report, the DoD IG indicates “Regarding the use of global settlements, unless the contract documents “such as negotiation memoranda” clearly detail the issues, amounts, and lines of accounting related to each item then the normal fund control visibility is not maintained.” The Department provided to the audit team accounting, contracting, and budget supporting data for each settlement to assist in validating the use of the FY2000 DHP Emergency Supplemental funding. The negotiation process included “bundling” of issues. This process precluded the assignment of lines of accounting for each element in the “bundled” settlement. While visibility to a finite level of detail is important, bilateral negotiation on each bundled issue did not occur and is therefore not trackable. Contracting officers are clearly responsible for negotiating fair and equitable settlements for the government and did so in the MCS contract global settlements. The bundling technique precluded assignments of lines of accounting for every issue.

Audit Team Members

The Finance and Accounting Directorate, Office of the Assistant Inspector General for Auditing, DoD, prepared this report. Personnel of the Office of the Inspector General, DoD, who contributed to the report are listed below.

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